

interLATA rivals. [FN215]

d. Commerce

44. Many commenters that address this issue, including DOJ, argue that the BOC interLATA affiliates should be classified as dominant only if they have the ability to raise the prices of interLATA services by restricting their own output. [FN216] DOJ and AT&T contend, however, that we should also classify a BOC interLATA affiliate as dominant if or (or its BOC parent) has the ability to seize the costs or restrict the output of the affiliate's rivals through control of an essential input, such as exchange access, or the ability to raise the prices paid by the affiliate and its rivals for exchange access. [FN217] DOJ claims that, even if consumer driven rates are not immediately, a BOC's ability to impose excessive costs on or to restrict essential inputs to its interexchange rivals presents a tool our law to combat it but however it will make the BOC's rivals weaker competitors, and thereby reduce their output and make consumer price increases inevitable. [FN218] DOJ asserts that raising rivals' costs is, in fact, likely to result in an increase in the BOC interLATA affiliate's rates, which could be prevented by dominant carrier regulation. [FN219]

e. Discussion

45. We conclude that the BOC interLATA affiliates should be designated as dominant carriers in the provision of intra-region, interstate, domestic, interLATA services only if the affiliates have the ability to raise prices of those services by restricting their own output on those services. As we stated in the Notice, we believe that our dominant carrier regulations are generally designed to prevent a carrier from raising prices by reducing its output rather than to prevent a carrier from raising its prices by raising its rivals' costs. [FN220] In fact, these regulations were designed at a time when AT&T was essentially a monopoly provider of domestic long distance services. [FN221] As discussed below, application of these regulations to a carrier that does not have the ability to raise long distance prices by restricting its own output could lead to injurious results. [FN222]

46. Even AT&T acknowledges that at least some of the dominant carrier regulations, such as price capping and more stringent section 214 requirements, are not designed to address the potential problems associated with BOC entry into competitive markets. [FN223]

For example, although we recognize, as discussed below, that there are circumstances in which price cap regulation (including price floors) on a BOC interLATA affiliate's rates might decrease a BOC's ability to engage in anticompetitive conduct, [FN224] we believe that in this situation the disadvantages of price cap regulation outweigh its benefits. Similarly, we question whether more stringent section 214 requirements would be an efficient means of addressing the concerns raised by BOC entry. Congress started the telecommunications authorization requirement in section 214 and subsequent amendments primarily to prevent investment in unnecessary new plant by rate-base regulated common carriers and to bar service discontinuance if a town served by a single carrier. [FN225]

Because we previously have found that markets for long distance services are substantially competitive in most areas, marketplace forces should effectively deter carriers that face competition from engaging in the practices that Congress sought to address through the section 214 requirements. For example, a carrier taking consignment links the incentive to invest in unneeded facilities, because it cannot extract additional revenue from its long distance customers to recover the cost of those facilities. [FN226] To such a carrier discontinuance service in an area where it faces competition, its customers would turn to the carrier's competitors for service. Because marketplace forces

Carrier affiliated. [FN368]

121. Some commenters assert, however, that a BOC could engage in a price squeeze without raising the price of its access services. These commenters suggest that, because access services are currently priced above economic cost, a BOC interLATA affiliate could set its interLATA prices at or below the BOC's access prices and still be profitable. [FN369] The affiliate's interLATA competitors would then be faced with the choice of setting their prices at unprofitable levels or losing market share. Several BOCs contend that this would not be a profit maximizing strategy because the increased revenues they could receive from the affiliate's interLATA services would be offset by a reduction in the access revenues received from nonaffiliated carriers. [Fn370] If the affiliate's reduction in interLATA rates did not fully increase demand, however, it is possible the BOC interLATA affiliate's higher interLATA revenues would more than offset lost access revenues, assuming the affiliate's interLATA competitors do not match the BOC's rates by reducing its. [FN371] If, in the alternative, the competitors reduce their interLATA rates to match the BOC interLATA affiliate's reductions, the BOC would receive increased access revenues. To the extreme, such a situation could drive the affiliate's rivals from the market. MCI claims that, even if such a predatory strategy is not successful, the rivals would be weakened by the cost increases they absorb, thereby reducing their output and their ability to compete effectively. [FN372]

122. We conclude that imposing advance notice and cost support data requirements on the BOC interLATA affiliates would not be an efficient means of preventing the BOCs from engaging in such a predatory price squeeze strategy.

[FN373] As previously discussed, advance notice periods for tariff filings could reduce the BOC interLATA affiliates' incentives to reduce their interLATA rates. Furthermore, requiring the BOC interLATA affiliates to file cost support data would discourage them from introducing innovative new service offerings. [FN374] We also conclude that imposing advance tariff filing and cost support data requirements on the BOC interLATA affiliates would not address LIMOS' concern that BOC interLATA affiliates could effectively evade imputation requirements by passing on their access cost advantage in reduced prices for services not subject to the Commission's jurisdiction, such as local exchange and information services. In addition, we believe that, if the predatory behavior described above were to occur, it could be adequately addressed through our complaint process and enforcement of the Antitrust Laws, coupled with the biennial audits required by section 272(d). [FN375] Such that the benefits of any protections offered by advance tariff filing and cost support data requirements would be outweighed by the enormous administrative burden those requirements would impose on the Commission. [FN376] A BOC interLATA affiliate that charges a rate for its interLATA services below its incremental cost to provide service would be in violation of sections 201 and 202 of the Communications Act, if such a rate were sustained for an extended period. [FN377]

123. We also note that other factors constrain the ability of a BOC or BOC interLATA affiliate to engage in a predatory price squeeze. For example, a BOC interLATA affiliate's apparent cost advantage resulting from its avoidance of access charges may be offset by other costs it must incur, such as the cost of interLATA transport, which, at least initially, may be greater than the true marginal cost of interLATA transport for tariff-based interLATA carriers. [FN378] In addition, a BOC interLATA affiliate will have to pay terminating access charges to BOCs other than its BOC parent for calls terminating outside the BOC's region and to competing LECs in the BOC's in-region states. Having to pay such access charges reduces the cost disparity between the BOC interLATA affiliate and competing interexchange carriers. Finally, we note that a price squeeze strategy would give a BOC interLATA affiliate the ability to raise price by restricting its own output only if it is able to drive competitors from the market. As discussed previously, the existence of four nationwide, or near-nationwide, network facilities makes it unlikely that a BOC interLATA affiliate could successfully engage in a predatory strategy. [FN379] As a result, we conclude that the BOCs or BOC interLATA affiliates will not be able

regulates BOC interLATA affiliates to file tariffs for interstate, domestic, intraexchange services, the ready availability of that information might facilitate tacit coordination of prices. We also believe that such requirements could impose significant administrative burdens on the Commission and the BOC interLATA affiliates, particularly if the extent they encourage the affiliated interLATA competitors to manipulate their interLATA rates in order to impede the affiliated's ability to compete. [FM240]

93. We find that the other regulations associated with dominant carrier telecommunications can also have undesirable effects on competition. Although a price floor might help prevent a BOC interLATA affiliate from pricing below its cost, a price floor, if set too high, could prevent consumers from enjoying lower prices resulting from real efficiencies. The required cost support data can also discourage the introduction of competitive new services or charges, because it requires a carrier to reveal its financial information to its competitors. [FM241]

94. As we discussed in the Notice, we believe that other regulation can appropriate to the BOCs and their interLATA affiliates will address the anticompetitive concerns raised in the Notice in a less burdensome manner. For example, a BOC's ability to engage in a "price squeeze" by raising its prices for access services [FM242] (as opposed to a BOC affiliate's lowering its long distance prices even when the BOC has not lowered its access prices) is limited by price cap regulation of those services. The non-discrimination and structural separation requirements set forth in section 702 and the rules thereunder, price cap regulation of the BOCs' exchange services were kept, and the Commission's anti-trust transaction rules sufficiently reduce the risk of inadvertent anticompetitive discrimination and improper allocation of market power. We agree with BOC that applying our local carrier regulation to an affiliate in a downstream market would be at best a clumsy tool for controlling vertical leveraging of market power by the parent, if the parent can be directly regulated instead. [FM243] In the Non-Accounting Safeguards Order and Accounting Safeguards Order, we adopted regulations to constrain the BOCs' ability to use their market power in local exchange and exchange access services to engage in anticompetitive conduct in competitive markets. We therefore reject AT&T and MCI's proposal that a BOC's ability to engage in such conduct would provide a legitimate basis for classifying its affiliate as dominant in the provision of in-region, interLATA, domestic, interLATA services.

95. We find that the entry of the BOC interLATA affiliates into the provision of interLATA services has the potential to increase price competition and lead to innovative new services and marketing efficiencies. [FM245] We see no reason to separate the BOC interLATA affiliates with regulations that are not well-suited to prevent the risks associated with BOC entry into in-region, interstate, domestic, interLATA services. We therefore conclude that the BOC interLATA affiliates should be classified as dominant carriers only if they have the ability to manage risk by restricting their own output.

3. Classification of BOC InterLATA affiliates in the Provision of In-Region, Interstate, Domestic, InterLATA Services

a. Regional Market Power Factors (Other than control of bottleneck facilities)

i. Background

96. In the Non-Accounting Safeguards DMR, we noted that, in determining whether a BOC possesses market power, the Commission has previously focused on certain well-established market factors, including market share, supply and demand substitutability, the cost structure, size or revenues of the firm, and control of

affiliates will not have the ability, upon entry or soon thereafter, to raise the price of in-region, interstate, domestic, interLATA services by reprofiting their own output, and, therefore, that the BOC interLATA affiliate should be classified as non-dominant in the provision of those services. We note, however, that we retain the ability to impose some or all of the dominant carrier regulations on one or more of the BOC interLATA affiliates if that proves necessary in the future. [FM387]

As discussed in the Notice, our experience with regulating the independent LBOC's provision of intrastate, domestic, interexchange services and the BOC's provision of enhanced services suggests that our existing safeguards have worked reasonably well, and generally have been effective, in conjunction with our regulatory advice, in deterring the improper allocation of costs and unlawful discrimination. [FM388] We are not persuaded by FCC's argument that the Ninth Circuit's decision in California IIT [FM389] leads to the conclusion that we should impose dominant carrier regulation on the BOC interLATA affiliates. [FM390] As discussed above, section 272 requires the BOCs to provide in-region, interLATA services through structurally separate affiliates. Since section 272's structural separation requirements are akin to those in Computer II, the Ninth Circuit's conclusion of whether the Commission had adequately justified its elimination of the Chapter 1 structural separation requirements for BOC enhanced services is not relevant here.

134. We believe that the entry of the BOC interLATA affiliates into the provision of in-region, interLATA services has the potential to increase price competition and lead to innovative new services and market efficiencies. We recognize that, as long as the BOCs retain control of local bottleneck facilities, they could potentially engage in improper cost allocation, discrimination, and other anticompetitive conduct to favor their affiliates' in-region, interLATA services. We acknowledge, however, that, to the extent dominant carrier regulation addresses such anticompetitive conduct, the burdens imposed by such regulation outweigh its benefits. We therefore see no reason to impose dominant carrier regulation on the BOC interLATA affiliates, given that section 272 contains numerous safeguards designed to prevent the BOCs from engaging in improper cost allocation, discrimination, and other anticompetitive conduct. [FM391]

We emphasize that our decision to accord non-dominant treatment to the BOCs' provision of in-region, interLATA services is predicated upon their full compliance with the structural, transactional, and nondiscrimination requirements of section 272 and our implementing rules. We believe that those safeguards, coupled with other statutory and regulatory safeguards, are sufficient to prevent the BOC interLATA affiliates from gaining the ability, upon entry or shortly thereafter, to raise prices by restricting their output.

a. Classification of BOC InterLATA Affiliates in the Provision of In-Region, International Services

b. Background

135. In the Non Accounting Safeguards RIM, we tentatively concluded that we should apply the same regulatory treatment to a BOC interLATA affiliate's provision of in-region, international services as we apply to its provision of in-region, interstate, domestic, interLATA services, assuming the BOC or BOC interLATA affiliate does not have an affiliation with a foreign carrier that has the ability to discriminate against the rivals of the BOC or its affiliate through control of bottleneck facilities in a foreign destination market. [FM392] Under this proposal, our current framework for addressing issues raised by foreign carrier affiliations would apply to the BOCs' provision of U.S. international services. [FM393]

b. Conclusion

the conclusion that the BOC interLATA affiliates will not have the ability to raise prices by restricting local output. Finally, given the presence of existing interexchange carriers, including such large well-established carriers as AT&T, MCI, Sprint, and Lucent, we find that the cost structure, size, and resources of the BOC interLATA affiliates are not likely to enable them to raise prices above the competitive level for their corporate interLATA services. [FM251] Although the BOC's brand identification and possible efficiencies of integration may give the BOC interLATA affiliates certain cost advantages in attracting customers, their lack of nationwide facilities-based networks would appear to put them at a disadvantage relative to the four largest interexchange carriers, as noted by Ameritech, particularly because the cost of resold long distance services will generally exceed the marginal cost of providing those services. [FM257]

b. BOC Control of Bottleneck Access Facilities

i. Background

18. In the Non Accounting Safeguards OMB, we noted that, in assessing whether a BOC interLATA affiliate would possess market power in the provision of in-region, interstate, domestic, interLATA services, we must also consider the significance of the BOC's current control of bottleneck exchange access facilities. [FM258] We noted the concern that a BOC's control of bottleneck access facilities would enable it to alleviate costs, improperly from its affiliate's interLATA services to the BOC's regulated exchange or exchange access services, discriminate against its affiliate's interLATA competitors, and potentially engage in a price squeeze against those competitors. [FM259] We therefore sought comment on whether the statutory and regulatory safeguards currently imposed on the BOCs and their affiliates are sufficient to prevent a BOC from engaging in such activities to such an extent that the BOC interLATA affiliates would quickly gain the ability to raise price by restricting output. [FM260]

ii. Comments

19. Some of the BOCs dispute the Commission's assumption that the BOCs have and will maintain control of bottleneck access facilities. These commenters argue that only controlled the BOCs may have once had in the exchange access market has been mitigated by the Commission's expanded interconnection initiatives, the 1996 Act, and the Commission's accompanying regulations, and the actions of various states. [FM261]

To contrast, AT&T contends that the BOCs' monopoly control over local bottleneck facilities gives them market power in the interexchange market. [FM262] Similarly, LOCS asserts that the BOCs will continue to possess market power in both the local exchange and exchange access markets, which translates into market power in the in-region interLATA market. [FM263] Very commenters also specifically address the three types of anticompetitive conduct listed above.

iii. Discussion

20. As argued in the Non Accounting Safeguards OMB, BOCs currently provide an overwhelming share of local exchange and exchange access services in areas where they provide such services—approximately 89.1 percent of the market, as measured by revenues. [FM264] Although the 1996 Act establishes a framework for eliminating entry barriers and thereby fostering local competition, the evidence

(Publication page references are not available for this document.)

control of bottleneck services or facilities in a foreign destination market. We will apply section 63.10(a) of our rules to determine whether we regulate a BOC international affiliate as a carrier on those U.S. international routes where an affiliated foreign carrier has the ability to discriminate against unaffiliated U.S. international carriers through control of bottleneck services or facilities in the foreign destination market. [FN404] The safeguards that we apply to carriers that we classify as dominant based on a foreign carrier affiliation are contained in Section 63.10(a) of our rules and are designed to address the incentive and ability of the foreign carrier to discriminate against the rivals of the U.S. affiliate in the provision of services or facilities necessary to terminate U.S. international traffic. [FN405] This framework for addressing issues raised by foreign carrier affiliations will apply to the BOCs' provision of U.S. international services as an additional component of our regulation of the U.S. international services market.

140. We reject NCI's suggestion that we should impose additional safeguards on the BOCs' intra-region international services. [FN406] We observe, as an initial matter, that all U.S. international carriers are subject to the same discrimination against "special concessions" from foreign carriers that we imposed on XET in the case approving XET's initial 20 percent investment in NCI. The grounding described by NCI would constitute a special concession prohibited by the terms of Section 63.10 of this Commission's rules to the extent the U.S. carrier entered into a grounding arrangement that the foreign carrier did not offer to similarly situated U.S. carriers. [FN407] A U.S. carrier that negotiates a grounding arrangement with a foreign carrier on a particular route would be required to submit the arrangement to the Commission for public comment and review in circumstances where this arrangement deviates from existing arrangements with other U.S. carriers and/or the routing and/or settlement of traffic on that route. [FN408]

141. We are not prepared to rule on this record, however, that the grounding of return traffic (i.e., giving a U.S. carrier the return traffic that terminates in a particular region) is a manner that may ultimately reduce U.S. carrier costs and rates in anti-competitive fashion. We recently adopted guidelines for permitting in certain circumstances flexible settlement arrangements between U.S. and foreign carriers that do not comply with the International Settlements Policy (ISP). [FN409] NCI & NII have apply ISP requirements to make our proceedings, with proper economic support, a true test of a BOC's intra-ATA and like or any other U.S. international carrier's seeks to establish an arrangement for grounding return traffic. [FN410]

142. We note when considering that the same conditions imposed in the 20 percent investment in NCI are useful or necessary in this case, NCI has not explained how those conditions are relevant to the BOC's intra-ATA affiliates' provision of intra-region international service on routes where they have no investment interest in or by a foreign carrier. The conditions imposed on XET apply to its operations only on the U.S.-U.K. route, where we found that XET controlled bottleneck local exchange and switching across facilities in the U.S. and, and they were targeted to limiting the potential risks of undue discrimination between a U.S. carrier (XET) and a foreign carrier with which the U.S. carrier has an equity relationship. [FN411] To the extent a BOC has an equity interest in a foreign carrier or the foreign carrier has some an interest in a BOC on a particular U.S. international route, it is of course subject to Section 63.10 of our rules. This rule sets forth the framework for imposing certain safeguards on U.S. carriers that are affiliated with foreign carriers that have the ability to discriminate in the favor of the U.S. affiliate through the control of bottleneck services or facilities. [FN412]

B. Classification of Independent BOCs

143. For the reasons discussed below, we conclude that the requirements established in the Fifth Report and Order, together with other existing rules,

(Publication page references are not available for this document.)

may, under certain circumstances, give the affiliate an unfair advantage over its competitors. [TM75] Recognizing this concern, Congress established safeguards in section 272, which we have implemented in the Non-Accounting Safeguards Order and Accounting Safeguards Order. For purposes of determining whether the BOC interLATA affiliates should be classified as dominant, however, we must consider only whether the BOCs might improperly allocate costs to such an extent that it would give the BOC interLATA affiliates, upon entry or soon thereafter, the ability to raise prices by establishing local cost control. We conclude that, in reality, such a situation could occur only if a BOC's improper allocation enabled a BOC interLATA affiliate to set lower interLATA prices at predatory levels (i.e., below the costs incurred to provide those services), drive out its Internet competitors, and then raise and sustain retail interLATA prices significantly above competitive levels. [TM76]

101. We conclude that applied to statutory and regulatory safeguards are likely to be sufficient to prevent the BOCs from improperly allocating costs between their long-distance exchange and exchange carrier services and their affiliates' competitive interLATA services to such an extent that their interLATA affiliates would be able to eliminate other interLATA service providers and subsequently earn supra-monopolistic profits by charging monopoly prices. Section 272(b) includes a number of structural safeguards that constrain a BOC's ability to allocate costs improperly. For example, the provision requires a BOC interLATA affiliate to "operate independently" from the BOC, [TM77] maintain separate books, records, and accounts from the BOC, [TM78] and have separate officers, directors, and employees. [TM79] Section 272 also requires each BOC to obtain and pay for a joint Federal Telephone audit every 3 years conducted by an independent auditor to determine whether each company has complied with [section 272] and the regulations promulgated under this section. [TM80] As noted by Ameritech and Bell Atlantic, the structural separation and audit requirements mandated in section 272 should reduce the risk of improper allocation of costs by minimizing the amount of illicit costs that would be improperly allocated. [TM81] In the Non-Accounting Safeguards Order, we adopted rules to implement and clarify these safeguards. For example, we concluded that the requirement that the BOC and its affiliate operate independently precludes the joint ownership of transmission and switching facilities by a BOC and its interLATA affiliate, as well as the joint ownership of the land and buildings where those facilities are located. [TM82] We also concluded that operational independence precludes a section 272 affiliate from performing operating, installation, and maintenance functions associated with the BOC's facilities. Likewise, it bars a BOC or any BOC affiliate, other than the section 272 affiliate itself, from performing operating, installation, or maintenance functions associated with the facilities that the section 272 affiliate owns or leases from a provider other than the BOC with which it is affiliated. [TM83] As noted by BellSouth, the separate employee requirement should ensure that the cost of each employee will be attributed directly to the appropriate entity. [TM84]

102. Section 272 also requires a BOC interLATA affiliate to conduct all transactions with the BOC on a uniform length basis, and all such transactions must be reduced to writing and made available for public inspection. [TM85] In the Accounting Safeguards Order, we conclude that, to satisfy this requirement, a section 272 affiliate must, at a minimum, provide a detailed written description of the asset or service transferred and the terms and conditions of the transaction on the Internet within 10 days of the transaction through the company's Internet home page. [TM86] We conclude that these safeguards will constrain a BOC's ability to allocate costs improperly and make it easier to detect any improper allocation of costs that may occur.

103. We further find that price cap regulation of the BOCs' access services reduces the BOCs' incentive to allocate improperly the costs of their affiliates' interstate services. As the Commission previously explained, "[b]ecause price cap regulation severs the direct link between regulated costs and prices, a carrier is not able automatically to recoup improperly allocated nonregulated costs by raising

Independent IFCs' provision of in-region, interstate, interexchange services. First, independent IFCs and others argue that the Commission should find that independent IFCs are non-dominant in their provision of in-region, interstate, interexchange services, and that the Fifth Report and Order requirements are no longer necessary. According to these commenters, the Commission should eliminate the existing Fifth Report and Order separate affiliate requirement as a precondition for non-dominant classification. [FN421]

In support of their contention that independent IFCs should be regulated as non-dominant in their provision of in-region, interstate, interexchange services, these commenters argue that: (1) independent IFCs do not have market power in the in-region, interstate, interexchange market based on the market power factors that the Commission applies in reclassifying AT&T as a non-dominant interexchange carrier; (2) dominant carrier regulation would reduce competition in the long distance market; (3) imposition of the Fifth Report and Order separation requirements on independent IFCs' provision of in-region, interstate, interexchange service is inconsistent with the 1996 Act; and (4) the real costs of requiring any level of separation for independent IFCs far outweigh the speculative benefits of regulation.

147. In addition, these commenters assert that independent IFCs have neither the ability nor the intent to leverage the market power resulting from their control over local facilities to impede competition in the interexchange market. [FN422] These commenters argue that their inability to leverage control over local facilities is attributable to several factors, including provisions of the 1996 Act that are designed to open the local market to competition, the geographic dispersion and largely rural nature of independent IFC service territories, [FN423], cost accounting safeguards, price cap on access services, and regulations to prevent local price discrimination in the quality of access services provided. [FN424] and the interexchange carriers' increasing emphasis on competing their own localities.

148. GTE argues that the Commission is legally prohibited from imposing separation requirements on independent IFCs in general, and specifically on CLE. GTE argues that section 251(a)(3) of the 1996 Act, which removes the restrictions and obligations imposed by the GTE Consent Decree, prohibits the Commission from applying any separate affiliate requirements on GTE. [FN425] In addition, CLE asserts that section 251 and 252 added by the 1996 Act, apply only to BOCs. Therefore, these sections reflect Congress' determination that there is no need to extend the separation requirements of section 254 to independent IFCs or GTE. [FN426] Moreover, GTE maintains that, if the Commission continues to require separate affiliates, it should modify the Fifth Report and Order requirements to allow the affiliate to take exchange access services not only by tariff, but also on the same basis as other carriers that have negotiated interconnection agreements pursuant to section 251. [FN427]

149. Sprint argues that the Fifth Report and Order separation requirements are no longer necessary because those requirements have been incorporated into the Commission's cost allocation rules. [FN428]

150. In contrast, interexchange carriers, except Sprint, and competing access providers generally argue that the Commission not only should retain the Fifth Report and Order separation requirements as a condition for non-dominant treatment of independent IFC provision of in-region, interstate, interexchange services, but also should impose additional safeguards to prevent independent IFCs from engaging in anti-competitive behavior by virtue of their control over bottleneck facilities. [FN429]

151. Teleport argues that the Commission should improve quarterly reporting requirements that will enable competitors and the Commission to analyze objectively the independent IFC's service record and to compare service to competitors with service to itself or its affiliates. [FN430] Teleport also recommends that the Commission implement an expedited complaint process to address service quality complaints by competing carriers. [FN431]

d. Unilateral Discrimination

i. Commerce

199. The BOCs suggest that concerns over the BOCs' incentives to discriminate are grossly exaggerated, given increasing competition in exchange and exchange access services (particularly after a BOC has satisfied the competitive checklist and other requirements in section 271); and the potential problem that customers would attribute degradation in service quality to the BOCs, rather than their interLATA affiliated competitors. [FN303] The BOCs further contend that, even if they did have the incentive to discriminate, they lack the ability to do so because of the nondiscriminatory requirement in the 1996 Act and because of engineering obstacles to own selective degradation of service quality. [FN304] Several BOCs also argue that discrimination is unlikely to be effective unless it is apparent to customers. According to the BOCs, if it is apparent to customers, however, it also is likely to be apparent to their long distance affiliated and regulators that have the authority to enjoin any illegal practices. [FN305] BellSouth and SBC contend that BOCs have a significant disincentive to provide inferior services to LDCs or otherwise jeopardize their relationship because the access charges paid by LDCs are a major source of revenue for the BOCs, and the LDCs increasingly will have the option of moving their exchange access traffic to alternative BOCs and LDCs. [FN306] Bell Atlantic and USIA claim that the BOCs have a long history of operating in other markets related to their local exchange and exchange access services without any adverse economic effects. They claim that, in each of the instances that the BOCs have been allowed to enter since divestiture -- cellular, voice messaging, customer premises equipment, and limited interLATA services -- output has grown, prices have fallen and consumers have thrived. [FN307] BellSouth asserts that, if such discriminatory behavior could happen, it would already have happened. [FN308]

200. A number of parties contend that, despite passage of the 1996 Act, BOCs have the incentive and ability to discriminate against their interLATA affiliates' long distance competitors. [FN309] AT&T argues that the BOCs can discriminate against interexchange competitors in numerous and subtle ways that would be difficult to police. [FN310] According to DOJ and Time Warner, the BOCs will retain the incentive and ability to discriminate against competitors until they are subject to actual, sustained competition in local telephone markets. [FN311]

ii. Discussion

201. In the Non-Discriminatory Referrals in IPPE, we noted that a BOC potentially could use its market power in the provision of local exchange and exchange access services to discriminate against its interLATA affiliate's interLATA competitors to gain an advantage for its interLATA affiliate. [FN312] We noted that there are various ways in which a BOC could attempt to discriminate against unaffiliated interLATA carriers, such as through poorer quality interconnection arrangements or unnecessary delays in satisfying its competitors' requests to connect to the BOC's network. [FN313]. Certain forms of discrimination may be difficult to police, particularly in situations where the level of the BOC's "cooperation" with unaffiliated interLATA carriers is difficult to quantify. To the extent customers value "one-stop shopping," degrading a rival's interexchange service may also undermine the attractiveness of the rival's interexchange/local exchange package and thereby strengthen the BOC's dominant position in the provision of local exchange services. [FN314]. We continue to be concerned that a BOC could attempt to discriminate against unaffiliated interLATA carriers. For purposes of determining whether the BOC interLATA affiliates should be classified as dominant, however, we need to consider only whether a BOC could discriminate against its affiliate's interLATA competitors.

GTE contends that, pursuant to the Commission's Rate Integration Order, [FM449] the integration of the Islands into domestic rate schedules is not required to occur until August 1, 1997. [PN669] GTE states that these off-island locations will continue to be classified as international points for rate purposes until that time. [FM4501]

C. Discussion

1. Traditional Market Power Factors (other than control of bottleneck facilities)

146. As we noted above, our own carrier regulation is generally designed to prevent a carrier from raising prices by restricting its own output of interexchange services. [FM451] An independent IEC, therefore, should be classified as dominant in the provision of in-region, interstate, interexchange services only if it has the ability to raise prices by restricting its output of those services.

147. We find that the traditional market power factors (excluding bottleneck control) suggest that independent IECs do not have the ability profitably to raise and sustain prices above competitive levels by restricting their output. Based on an analysis of these traditional market power factors -- market share, supply and demand substitutability, cost structure, size, and resources -- we conclude that independent IECs do not have the ability to raise prices by restricting their own output. [FM452] First, independent IECs generally have minimal market share, measured with the major interexchange carriers, which suggests they could not profitably raise and sustain interexchange prices above competitive levels. Second, the very high supply and demand elasticities that the Commission found constrained AT&T's pricing behavior also apply to independent IECs. Finally, we find that low entry barriers in the interexchange market and widespread use of interexchange services constrain independent IECs from exercising market power. We conclude, therefore, that in light of the Fifth Report and Order requirements independent IECs do not have the ability to raise prices above competitive levels by restricting their output of interexchange services.

2. Control of bottleneck access facilities

148. As we previously found with regard to the BOQ, traditional market power factors are not conclusive in determining whether independent IECs should be classified as dominant in the provision of in-region, interstate, interexchange services. [FM453] We noted in the Non-Accounting Safeguards [FM454] that an independent IEC may be able to use its control over intra-exchange and exchange access services to disadvantage its interexchange competitors to such an extent that it will quickly gain the ability profitably to raise the price of in-region, interstate, interexchange services above competitive levels. [FM455] We therefore must examine whether an independent IEC could improperly locate sites, discriminate against its in-region competitors, or engage in a price squeeze to such an extent that the independent IEC would have the ability to raise prices for interstate, interexchange services by restricting its output. [FM456] We find, as we did with regard to BOQs, that independent IECs providing in-region, interstate, interexchange services do not have the ability to engage in these actions to such an extent that they would have the ability to raise prices by restricting output. For the reasons discussed with regard to the BOQ, we thus conclude that dominant care or removal of independent IEC provision of in-region, interstate, interexchange services is inappropriate.

149. We disagree, however, with those commenters that assert that independent

affiliates received." [RM328]

117. We recognize that the nondiscrimination requirements in the Communications Act are effective only to the extent that they are enforced. To this end, the 1996 Act gives the Commission specific authority to enforce the requirements of section 272 and the other conditions for interconnection, interLATA entry incorporation in section 271(d)(3). [RM329]

Section 271(d)(6) provides that "[i]f at any time after the approval of a [BOC application under section 271(d)(3)], the Commission determines that a [BOC] has failed to meet any of the conditions required for such approval, the Commission may, after notice and opportunity for a hearing - (i) issue an order for such company to correct the deficiency; (ii) impose a penalty on such company pursuant to title V; or (iii) suspend or revoke such approval." [RM330] In the Non Accounting Safeguards Order, we concluded that this authority augments the Commission's existing enforcement authority. [RM331] Section 271(d)(6) also specifies that the Commission must act within 90 days on a complaint alleging that a BOC has failed to meet a condition required for its regional, interLATA approval under section 271(d)(3). [RM332]

118. In light of the 90-day deadline to rule upon a 271(d)(6) complaint, we adopted certain measures in the Non Accounting Safeguards Order to expedite the processing of these complaints. [RM333] For example, once a complainant has demonstrated a prima facie case that a defendant BOC has failed to meet the conditions of entry, the burden of production (i.e., coming forward with evidence) will shift to the BOC defendant. [RM334] By shifting this burden of production, we have placed on the BOC an affirmative obligation to produce evidence and argument necessary to rebut the complainant's prima facie case or face an adverse ruling. [RM335] In the Non Accounting Safeguards Order, we also concluded that, in addressing complaints alleging that a BOC has failed to meet the conditions required for the provision of in-region interLATA services, we will not apply a presumption of reasonableness in favor of the BOC interLATA affiliate, regardless of whether the BOC or BOC interLATA affiliate is regulated as a dominant or non-dominant carrier. [RM336] We believe that these enforcement mechanisms will allow us to adjudicate any signs against the BOCs and BOC interLATA affiliates in a timely manner.

119. We conclude that the statutory and regulatory safeguards discussed above will prevent a BOC from discriminating to such an extent that its interLATA affiliate would have the ability, upon entry or shortly thereafter, to raise the price of in-region, interstate, domestic, interLATA services by restricting its output. [RM337] We also conclude that imposing dominant carrier regulation on the BOC interLATA affiliate would not significantly aid in the prevention of most types of discrimination. [RM338] Although AT&T expresses concern about the risk of discrimination, it suggests that the Commission should impose stringent non-discrimination requirements and reporting obligations in order to combat this problem. It does not contend that dominant carrier regulation would help to prevent discrimination. [RM339] We are not persuaded by Tim McNeer's assertion that dominant carrier regulation is necessary to ensure that the BOCs comply with their statutory obligation to charge off-exchange rates equal to those charged unregulated carriers for telephone exchange and exchange access services. [RM340] Rather, as discussed above, we conclude that the section 272 safeguards, coupled with the expedited enforcement mechanism, should provide an adequate means of ensuring that the BOCs comply with this requirement.

v. Price Squeeze

vi. Crossroads

120. The BOCs generally argue that they do not have the ability to engage in a

services to be taken at tariffed rates, or as discussed below, on the same basis as requesting carriers that have negotiated interconnection agreements pursuant to section 251. (FN46) This is preventing a BOC from discriminating in favor of its long distance affiliates, and reduces somewhat the risk of a price squeeze in the extent that an affiliate's long distance prices are required to exceed their costs for tariffed services. (FN47)

186. We agree that we should modify the third FIFTH Report and Order requirement for a local independent LECs to take exchange services not only by tariff, but also on the same basis as requesting carriers that have negotiated interconnection agreements pursuant to section 251. (FN48) ~~BOC carriers that, because under the Commission's current rules, LBOCs must make interconnection agreements available to other carriers, (FN49) affiliated carriers should be able to take LBOC services under such as we we well. (FN50)~~ In the Non Accounting Safeguards Order, we conclude that section 272 does not prohibit a BOC from taking LBOC services from providing local exchange services in addition to intrastate services. (FN51) We also found in that Order that section 251 does not place any restriction upon the telecommunications carriers may qualify as requesting carriers. (FN52) We concluded in the Non Accounting Safeguards Order, therefore, that BOC section 272 affiliations should be permitted to provide unbundled elements under section 251(a)(3) of the Communications Act and telecommunications services at wholesale rates under section 251(c)(4) from the BOC on the same terms and conditions as other competing local exchange carriers. (FN53) We find no basis for concluding that Congress intended to treat an incumbent LBOC differently from any other requesting telecommunications carrier. Accordingly, in addition to taking exchange services by tariff, the LBOC may alternatively take unbundled network elements or exchange services for the provision of a telecommunications service, subject to the same terms and conditions as provided in an agreement approved under section 253 to which the independent LBOC is a party.

187. As argued by many commenters, independent LBOCs have been providing intraregional interexchange services on a separate basis with no substantiated complaints of denial of access or discrimination. The Fifth Report and Order separation requirements have been in place for over ten years. During that time, we have received few complaints from independent LBOCs about the requirements themselves. Moreover, we previously determined that the Fifth Report and Order requirements are not overly burdensome. As we stated in the Interim BOC Out-of-Region Order, the separation requirements of the Fifth Report and Order require that the LBOC interexchange affiliate be a separate legal entity. We do not, however, require actual "structural separation." (FN54) Thus, as we stated in the Interim BOC Out-of-Region Order, "except for the ban on joint ownership of transmission and switching facilities," the LBOC and the interexchange affiliate "will be able to share personnel and other resources or assets." (FN55)

188. We are not persuaded by the arguments made by Citizens and USTA that the separate LBOC rate requirement prevents independent LBOCs from realizing efficiency gains through the use of joint resources. (FN56) While joint ownership of transmission and switching facilities by a LBOC and its affiliate is not permitted by our rules, the use of transmission and switching facilities by the other is permissible. The affiliate can contract for use of the LBOC's transmission and switching facilities at tariffed rates or on the same basis as requesting carriers that have negotiated interconnection agreements pursuant to section 251. (FN57) and thereby continue to benefit from economies of scope. Furthermore, we conclude that the separate books of account requirement and the requirement that the affiliate obtain LBOC services at tariffed rates are not overly burdensome. As we explained in the Interim BOC Out-of-Region Order, "the separate books of account requirement refers to the fact that, as a separate legal entity, the affiliate must maintain its own books of account as a matter of course." (FN58) Moreover, as we also previously, in addition to taking exchange services by tariff, to the extent that the independent LBOC affiliate meets the requirements of 251, the LBOC affiliate may alternatively take unbundled network elements or exchange services subject to

below cost without incurring a loss. According to Ameritech, any subsidies in advance are real costs that the BOC must recover in some manner in order to remain "whole." Ameritech also claims that price squeeze arguments ignore the fact that BOC interLATA affiliates will pay access charges to unaffiliated carriers when they originate or terminate long distance calls out-of-region and that facilities based in local carriers actually have significant cost advantages. [FN355]

Firstly, Ameritech disputes the relevance of the price squeeze arguments. According to Ameritech, a BOC interLATA affiliate's ability to gain market share by setting rates below the cost of service would not constitute a basis for classifying the BOC interLATA affiliate as dominant. [FN357] Ameritech is aware of no "legit" theory under which such a practice could be considered unreasonable or otherwise unlawful, since consumers would suffer no harm unless the BOC interLATA affiliate could somehow acquire market power from its service. [FN358] Bell Atlantic and AT&T claim that advance notice periods for tariff filings and cost support requirements are unnecessary to ensure compliance with the section 272 imposition requirements because the 1996 act already provides for a biennial audit, which is intended to serve specifically as a check on compliance with the section 272 separation requirements, including the imposition requirement. [FN359]

II. Discussion

120. In the Non-Bundling of Safeguards NPM, we noted that, absent appropriate safeguards, a BOC potentially could raise the price of access to all interexchange carriers, including its affiliate. [FN360] This would cause competing interLATA carriers either to raise their retail interLATA rates in order to maintain the same profit margins or to downplay its market share by not raising their prices to reflect the increase in access charges, thereby reducing their profit margins. [FN361] If the competing in-region interLATA service providers raised their prices to recover the increased access charges, the BOC interLATA affiliate would seek to expand its market share by not matching the price increase. In that event, although the BOC interLATA affiliate would achieve lower profit margins than its rivals, all other things being equal, the BOC corporate entity as a whole would receive additional access revenues from unaffiliated carriers due to the access price increase and greater revenues from the affiliate's interLATA services caused by the increased share of interLATA traffic. If the BOC were to raise its access rates high enough, it would be impossible for interexchange competitors to compete effectively. Thus, the entry of a BOC's affiliate into the provision of in-region interLATA services might give the BOC an incentive to raise the price for access services in order to disadvantage its affiliate's rivals, increase its BOC's market share, and increase the profits of the BOC overall. [FN362].

121. We conclude, as discussed in the Notice, that price cap regulation of the BOC's access services sufficiently constrains a BOC's ability to raise access prices to such an extent that the BOC affiliate would gain, even entry or soon thereafter, the ability to raise prices of interLATA services above competitive levels by restricting its own output of those services. [FN363] Although a BOC may be able to raise its access rates to some extent if those rates are currently below the applicable service cap and could fail to pass along reductions in the cost of access if the productivity factor is too low, [FN364] we conclude that such an increase would not give a BOC affiliate the ability to raise prices of interLATA services above competitive levels by restricting its own output of those services. [FN365] We will consider the impact of such a potential increase on competition in the pending access charge reform proceeding. We also note that the ability of competing carriers to acquire access through the purchase of unbundled elements enables them to avoid originating access charges and thus partially protect themselves against a price squeeze. [FN366] To the extent that access charges are intended to more closely reflect economic cost, [FN367] as is being considered in the access charge reform proceeding, the potential for a price squeeze should be

(Publication page references are not available for this document.)

services areas. In addition, because the service areas of independent LECs tend to be smaller than the service areas of the BOCs, on average, independent LECs have fewer local lines per switch than BOCs and provide relatively little interexchange traffic that both originates and terminates in their region. [FN456] We conclude, therefore, that independent LECs are less likely to be able to engage in anticompetitive conduct than the BOCs and that applying the section 272 requirements to independent LECs would be overly burdensome. The Fifth Report and Order ("the elements appear to balance these competing concerns; they address cost shifting and discrimination, but do not appear to be overly burdensome." [FN487]) although the independent LECs assert that these requirements "increase their costs, none of them has provided specific evidence to support this claim, much less to demonstrate that these additional costs outweigh the benefits."

171. As previously stated, we conclude that we should not apply dominant carrier regulation to independent LECs. The dominant carrier regulation that AT&T and KCR recommend is not necessary to prevent, nor effective in detecting improper cost allocation, unlawful discrimination, price squeezes, or other anticompetitive conduct. [FN488] The benefits of dominant carrier regulation are outweighed by the burdens imposed on independent LECs. [FN489] We also reject AT&T's argument that we should maintain full dominant carrier regulation in order to enforce effectively the Commission's imputation requirements and to prevent independent LECs from engaging in a price squeeze strategy. As we stated previously, we believe that such predatory behavior can be adequately addressed through our complaint process and enforcement of the antitrust laws. [FN490] Moreover, we note that the potential for a price squeeze will be further mitigated as access charges are referred to reflect cost. [FN491]

172. Furthermore, we confirm that the equal access restrictions apply to independent LECs. [FN492] Under the MET the BOCs were required to "provide to all interexchange carriers and information service providers exchange access, information access and exchange services for local access on an unbundled, tariffed basis, that is, equal in type, quality, and price to that provided to AT&T and its affiliates." [FN493] Equal access involves the simultaneous provision of exchange access services, signaling parity, and crossconnection of interexchange carriers. [FN494] Exchange access services included, but were not limited to, provision of network control signaling, answer supervision, accounted calling number identification, carrier access codes, directory services, naming and maintenance of facilities, and the provision of information necessary to bill customers. [FN495] The became subject to a similar requirement in 1984. [FN496] and in 1993 the Commission imposed requirements on independent LECs similar to those imposed on BOCs. [FN497] As we stated in the Non-Autonumbering Safeguards Order, section 2(1)(g) added by the 1993 Act preserves the open access requirements in place prior to the passage of the Act, including obligations imposed by the BOC and any transition rules. [FN498] We do not decide at this time, however, whether the allegations AT&T raises regarding SNET's alleged non-prescribed interexchange carrier (PTC) "freeze" plan constitutes a violation of the Commission's equal access requirements. [FN499] AT&T or any other carrier, if it deems appropriate, can file a complaint with the Commission raising this allegation in the proper context. [FN500]

173. Based on the foregoing, we conclude that we should require independent LECs to provide in-region, interstate, interexchange services through a separate affiliate that satisfies the Fifth Report and Order separation requirements. We further conclude that, in light of our finding that independent LECs do not have the power to judge and sustain interexchange rates above competitive levels, it would be inconsistent with our analysis to allow independent LECs to choose whether to be regulated as a dominant carrier when providing in-region, interstate, domestic interexchange services. We are aware, however, of three independent LECs, Union Telephone Company (of Wyoming) (Union), GTE Hawaiian Tel., and MTC, that currently provide interexchange services on an integrated basis subject to dominant carrier regulation. We recognize that the costs of complying with the Fifth Report and

to extend is a price squeeze to such an extent that the BOC's interLATA affiliate will have the ability, upon entry or soon thereafter, to raise price by restricting their own output. Thus we do not believe that classifying a BOC's interLATA affiliate as a dominant carrier is necessary or appropriate to constrain the BOC and its affiliate from attempting to execute a predatory price squeeze.

130. We agree with commenters that suggest that the risk of the BOC's engaging in a price squeeze will be greatly reduced when interLATA competitors gain the ability to purchase access to the BOC's networks at or near cost, and as competition develops in the provision of exchange access services. [RM380] As noted, we believe that the ability of competing carriers to acquire access through the purchase of unbundled elements enables them to avoid originating access charges and thus partially protect themselves against a price squeeze. Moreover, to the extent that access charges are reformed to more closely reflect economic cost, as is being considered in the access charge reform proceeding, the concern for a price squeeze should be further alleviated. [RM381]

f. Mergers or Joint Ventures Between Two or More BOCs

i. Background and Comments

131. In the Non-Accounting Safeguards Notice, we sought comment on what effect, if any, a merger of or joint venture between two or more BOCs would have on our determination as to whether to classify the interLATA affiliate of one of those BOCs as non-dominant or non-dominant. [IN182] Bell Atlantic, comments that the prospect of mergers between BOCs should not have any impact on whether the BOCs are treated as dominant because both parties to such a merger would be entering the long distance market with zero market share and in competition with well established monopolists and because the merged company's access by nature would remain subject to all the same market and regulatory constraints as unmerged BOCs. [RM383] Sprint and the New York State Department of Public Service (NYDPS) concluded that mergers, acquisitions, and similar combinations by BOCs may require consideration of geographic markets more expansive than a particular BOC's region. [RM384]

ii. Discussion

132. We conclude that a merger of or joint venture between two or more BOCs should have no direct effect on our determination of whether to classify the interLATA affiliates of one of those BOCs as dominant or non dominant. Bell Atlantic notes that, even though a merged entity's market would grow, it would continue to be subject to the same regulation currently imposed on the individual companies prior to the merger or joint venture. In the Non-Accounting Safeguards Notice, we concluded that, upon completion of a merger between or among BOCs, the non-regulatory unit of a merged entity shall include all of the in-region states of each of the BOCs involved in the merger. [RM385] Thus, the merged entity would be required to satisfy the requirements of sections 271 and 272 in providing interLATA services originating in those in-region states. We also note that BOC is currently considering the implications of such mergers and joint ventures from an antitrust perspective. [RM386]

g. Conclusion

133. Based on the preceding analysis, we conclude that the BOC's interLATA

a. Commerce

177. NCAI agrees with the tentative conclusion that only those independent LECs that control local exchange or exchange access facilities should be subject to the requirements adopted in this proceeding and that the Commission should rely on the definition of "incumbent local exchange carrier" provided in 47 U.S.C. § 251(b). [PM909.]

178. NICA, on the other hand, contends that the Commission should treat new entrants no differently than it treats small incumbent LECs because new LEC entrants that provide in-region interexchange services are free to, and have in fact, built or acquired control of local exchange access facilities. [S0509.]

b. Disagreed

179. We adopt our tentative conclusion that the Fifth Report and Order separation requirements should be imposed only on incumbent independent LECs that control local exchange and exchange access facilities. We believe this conclusion is consistent with the 1996 R.R., which provides different regulatory treatment for incumbents and non-incumbent LECs. [PM910] This different treatment generally imposes fewer regulatory requirements on non-incumbent LECs, which we believe indicates Congress's view that such carriers are unable, at this time, to exert unacceptably adverse effects and therefore, are unable to generally harm consumers through unreasonable rates. We also believe that it would be premature to impose such regulation on competitive LECs when they possess little, if any, market power in the local exchange at this time. By limiting application of the separation requirements to incumbent independent LECs that control local exchange and exchange access facilities, we avoid imposing unnecessary regulation on new entrants in the local exchange market, such as neighboring LECs, interexchange carriers, cable television companies, and commercial mobile radio service providers, some of which may be small entities, thus facilitating market entry and the development of competition in the in-region, intrastate, domestic, interexchange market.

c. Application of Fifth Report and Order Separation Requirements to Small or Dual-Independent Independent LECs

a. Background

180. In the Non Accounting Safeguards NRRM, we sought comment on whether there is some minimum size for independent LECs below which the separation requirements should not apply. We noted that, in principle, the size of a LEC will not affect its incentives to improperly allocate costs between its monopoly services and its competitive services, but that for one or more independent LECs, the benefits to ratepayers of a separate affiliation requirement may be less than the costs imposed by such a requirement.

b. Commerce

181. Several commenters contend that we should exempt very small or dual-independent LECs (e.g., non-Class A LECs or LECs serving less than two percent of

188. Most commenters support the Commission's proposal to apply the same regulatory treatment to the BOC interLATA affiliates' provision of in-region, international services as it applies to in-region, interstate, domestic interLATA services. [FM394] PacTel and T S West agree that if the BOC interLATA affiliates should be non-dominant for in-region domestic services, they should be non-dominant for in-region international services, but they further claim that differences in the domestic and international markets suggest that BOC interLATA affiliates should be classified as non-dominant for international interLATA services regardless of their classifications for domestic services. [FM395] PacTel agrees that the existing rules governing dominance based on foreign market affiliations should apply to BOC interLATA affiliates as they do to all other international carriers. PacTel suggests, however, that the Commission should ensure that route-by-route dominance (in-region, foreign or foreign affiliations) be concluded no later than the grant of a new or BOC entry permit. [FM396]

189. NCT generally agrees with the Commission that a BOC's in-region international service should be treated in a manner similar to its in-region interstate interLATA service. [FM397] It contends, however, that the BOCs have unique advantages in the international services market as a result of their regional focus. NCT expresses concern that the BOCs will enter into specific arrangements with foreign carriers under which certain traffic would be "groomed" -- i.e., the foreign carrier would give the BOC's interLATA affiliate the return traffic that terminates in the BOC's region. [FM398] NCT contends that, by contrast, two-BOC interexchange carriers would be required to take return traffic to destinations all over the United States and thereby incur higher costs in terminating such traffic. NCT notes that a prospect could expect of international traffic terminators in the AMERI and Pacific Bell regions and argues that these BOCs would have an especially lucrative opportunity to obtain groomed traffic. [FM399] NCT notes that such arrangements may result in lower costs for terminating U.S. inbound traffic, but characterizes those arrangements as "anti-competitive." It urges the Commission, at a minimum, to impose on the BOC interLATA affiliates the same requirements that it imposed on NCT in the order approving British Telecom's (BT's) initial 25 percent investment in BOC. [FM400] A number of the BOCs respond that such additional requirements are unnecessary and inappropriate. [FM401].

a. Discussion

190. We adopt our tentative conclusion that we should apply the same regulatory treatment to a BOC interLATA affiliate's provision of in-region, international services as we apply to the provision of in-region, interstate, domestic, interLATA services. As discussed in the Notice, the relevant issue in both contexts is whether the POC interLATA affiliate can exploit its market power in local exchange and exchange access services to raise prices by restricting its own output in another market (the domestic, in-interLATA or international markets). We also note that the section 702 safeguards apply equally to the BOCs' in-region, domestic, interLATA and in-region, international services. [FM402] We find no practical distinctions between a BOC's ability and incentive to use its market power for the provision of local exchange and access services to improperly allocate costs, discriminate against, or otherwise disadvantage unaffiliated domestic interexchange competitors as opposed to international service competitors. [FM403].

191. In light of our classification of the BOC interLATA affiliates as non-dominant in the provision of in-region, interstate, domestic, interLATA services, we accordingly will classify such BOC interLATA affiliates as non-dominant in the provision of in-region, international services, unless it is affiliated, within the meaning of section 63.19(b)(1)(i) in our rules, with a foreign carrier that has the ability to discriminate against the rivals of the BOC or its affiliate through

In Fifth Report and Order requirements on independent LECs providing either long-distance or international interexchange services because independent LECs do not have market power in the provision of domestic or international in-region interexchange services. GTE notes that it, and some other carriers, may be subject to dominant classification on particular routes pursuant to the Foreign Carrier Entry Order due to foreign carrier affiliations. [FN521]

FCC, on the other hand, argues that the Commission should generally apply the same regulatory treatment to independent LECs' provision of in-region, international services, but impose additional requirements where the LEC has a foreign with the ITC or other commercial relationship with a foreign carrier. [FN522] FCC urges the Commission, at a minimum, to impose on the independent LEC in such circumstances the same safeguards that it imposed on AT&T in the Order approving British Telecommunications' (PTT's) initial 20 percent investment in MCI. [FN523]

Mr. Inada also, CNM asks the Commission to clarify that AT&T is a dominant carrier under the terms of the International Competitive Carrier Order. [FN524] CNM states that in the International Competitive Carrier Order, the Commission ruled that MCI's parent company, GTE Hawaii, and similarly situated carriers were dominant. CNM claims, however, that AT&T was not covered by those policies when the Commission issued this order because CNM did not become a U.S. company until November 5, 1986. [FN525] CNM asserts that, now that AT&T is a domestic carrier with significant market power and a lack of effective competition in exchange and exchange access markets, the Commission should declare AT&T dominant in the provision of in-region, interstate, international, interexchange service. [FN526] GTE replies that imposing dominant regulation on AT&T's provision of in-region, interstate, international, interexchange services now, when MCI has operated as non-dominant for years, [FN527] would be contrary to the deregulatory goals of the 1986 Act. [FN528] In any case, GTE asserts that independent LEC international and domestic interexchange services should be regulated in the same manner and that independent LECs have no market power in the international service market. GTE further argues that AT&T's exchange access service in the Northern Mariana Islands cannot give it market power in the international services market. [FN529]

IV. Discussion

183. We confirm our tentative conclusion that we should adopt the same rules in this proceeding for an independent LEC's provision of in-region, international, interexchange services as we except for its provision of local, regional, interstate, domestic, interexchange services. As discussed above with regard to BOC provision of in-region, international services, the relevant issue, with respect to both domestic interexchange and international services, is whether an independent LEC can exercise its market power in local exchange and exchange access services to raise and sustain prices of interexchange or international services above competitive levels by restricting its own output. [FN530] We find no practical distinctions between an independent LEC's ability and incentive to use its control over bottleneck facilities in the provision of local exchange and exchange access services to improperly allocate costs, unreasonably discriminate against, or otherwise engage in anticompetitive conduct against affiliated domestic interexchange competitors as opposed to international service competitors.

183. In light of our decision to classify independent LECs as non-dominant in the provision of in-region, interstate, domestic, interexchange services and to impose the Fifth Report and Order requirements, we will classify an independent LEC as non-dominant in the provision of in-region, international services, unless it is affiliated with a foreign carrier that has the ability to discriminate in favor of the independent LEC through control of bottleneck services or facilities in a foreign destination market. [FN531] We will apply section 63.1(c)(1) of our rules to determine whether to regulate a independent LEC as dominant in those U.S.

(Publication page references are not available for this document.)

sufficiently limit an independent LEC's ability to exercise its market power in the local exchange and exchange access markets so that the LEC cannot profitably raise and sustain the price of in-region, interstate, domestic, interexchange services by restricting its own output. We, therefore, classify independent LECs as non-dominant in the provision of these services. We recognize, however, that an independent LEC conceivably could use its control over local bottleneck facilities to abuse its market power, engage in unlawful discrimination, or attempt to price squeeze. We, therefore, impose the Fifth Report and Order separation requirements on all independent LECs that provide in-region, interstate, domestic, interexchange services. We further conclude that we should apply the same regulatory classification to the independent LECs' provision of in-region, interstate, domestic, interexchange services.

3. Classification of Independent LECs in the Provision of In-Region, Interstate, Domestic, Interexchange Services

a. Background

[344] In the Competitive Carrier Tariff Report and Order, the Commission determined that interexchange carriers affiliated with independent LECs would be regulated as non-dominant carriers. [30417] In the Competitive Carrier Fifth Report and Order, the Commission clarified the definition of tariffed rate¹⁴ and identified three separation requirements that the affiliate must meet in order to qualify for non-dominant treatment. These requirements are that the affiliate: (i) maintain separate books of account; (ii) not jointly own or co-own or co-control switching facilities with the LEC; and (iii) acquire any services from its affiliated exchange company at tariffed rates, terms, and conditions. [34415] The Commission further concluded that, if the LEC provides interstate, interexchange service directly, rather than through an affiliate, or if the affiliate fails to satisfy the three requirements, those services would be subject to dominant carrier regulation. [30416] The Commission observed that these separation requirements would provide some "protection against cost-shifting and anti-competitive conduct" by an independent LEC that could result from its control of local bottleneck facilities. [30417]

[345] In the Non-Accounting Safeguards NRM, we sought comment on how we should classify independent LECs' provision of in-region, interstate, domestic, interexchange services. We also sought comment on whether, absent the Fifth Report and Order separation requirement, an independent LEC would be able to use its market power in local exchange and exchange access services to disadvantage its interexchange competitors to such an extent that it would quickly gain the ability profitably to refine and sustain the price of in-region, interstate, domestic interexchange services significantly above competitive levels by restricting its output. [30418] We suggested that, regardless of our determination of whether independent LECs should be classified as dominant or non-dominant, some level of separation may be necessary between an independent LEC's interstate, domestic, interexchange operations and its local exchange operations to guard against cost misallocation, unlawful discrimination, or a price squeeze. [30419] In addition, we sought comment on whether the existing Fifth Report and Order requirements are sufficient safeguards to apply to independent LECs to address these concerns. [30420]

b. Comments

[346] Commenters generally suggest two different schemes for regulating

other type of sunset.

A. Comments

174. Frontier contends that we should eliminate any separation requirements applicable to independent IECOs' provision of in-region, interstate, interexchange services no later than such time as section 272 requirements sunset. [FN533]

175. SPRINT and CMMI oppose the removal of the separate affiliate requirements applicable to independent IECOs. [FN541] CMMI notes that the sunset provision in section 272 has no application to independent IECOs. Moreover, CMMI states that in insular areas such as the Commonwealth, there is no evidence to suggest that effective local competition will develop in the near future. [FN542]

B. Discussion

176. We intend to commence a proceeding three years from the date of adoption of this Order to determine whether the emergence of competition in the local exchange and interexchange access marketplace justifies removal of the Fitch Report and Order requirements. [FN543] We believe that three years should be a reasonable period of time in which to evaluate whether effective competition has developed sufficiently to reduce or eliminate an independent IECO's bottleneck control of exchange and exchange access facilities.

B. CLASSIFICATION OF BOCs AND INDEPENDENT IECOs AS DOMINANT OR NON-DOMINANT IN THE PROVISION OF OUT-OF-REGION INTERSTATE, DOMESTIC, INTEREXCHANGE SERVICES

177. In this section, we consider whether the Competitive Carrier Fifth Report and Order separation requirements that were applied to the provision of out-of-region, interstate, domestic, interexchange services by independent IECOs in the Competitive Carrier proceeding and to the provision of such services by the BOCs in the Interim IECO Out-of-Region Order are necessary as a condition to non-dominant regulatory treatment. As discussed below, we conclude that BOCs and independent IECOs do not have and will not gain the ability in the near term to use their market power in the provision of local exchange service in their in-region markets to such an extent that the BOCs or independent IECOs could significantly raise and sustain prices for out-of-region, interstate, domestic, interexchange services significantly above competitive levels by restricting their own output. We therefore classify the BOCs and independent IECOs as non-dominant in the provision of these services. We also conclude that at this time, a BOC or an independent IECO will not be able to raise significantly the interexchange carriers' costs by improperly allocating costs from its out-of-region local exchange services to its regulated exchange and exchange access services, unfairly discriminating against its rivals, or engaging in a price squeeze on the provision of out-of-region, interstate, domestic, interexchange services. We therefore eliminate the separation requirements imposed in the Fitch Report and Order as a condition for non-dominant regulatory treatment of the BOCs and independent IECOs in the provision of these out-of-region services.

A. Background

178. As previously noted, the Commission determined in the Competitive Carrier proceeding that interexchange carriers affiliated with independent IECOs would be

152. AT&T argues that the Fifth Report and Order and our dominant carrier requirements are inadequate to address independent IECs' potential abuse of market power. [FN432] AT&T contends that the Commission should, therefore, impose the same structural separation and non-discrimination requirements on independent IECs that we impose on BOCs, as well as a modified form of dominant carrier regulation. AT&T also asks the Commission to make clear that equal access requirements apply to independent IECs, including the requirement that a customer seeking local service from such carriers be offered the option for interexchange service in a neutral fashion. [FN433] AT&T asserts that the Fifth Report and Order allows joint and integrated design, planning, and provisioning of exchange and interexchange services, which inherently discriminates against other carriers and permits the costs of long distance operations to be misallocated to monopoly ratepayers. [FN434] In addition, AT&T, challenging SNET's claim that geographic rate averaging would mitigate the effects of any unilateral increase in access charges, asserts that access charges are far above cost, and that this enables BOCs to impose a price squeeze in the interexchange market. [FN435]

153. BOC asserts that, given the types of abuses that control over bottleneck facilities allows, it is necessary to revise independent IECs' ITU-regime interexchange rates to ensure that they fully cover independent IECs' imputed access and other costs. [FN436] BOC further contends that enforcement of the imputation requirement is necessary to protect against an independent IEC's adopting a price squeeze strategy. [FN437] and maintains that the Commission's cost accounting rules and after the fact audits are insufficient to ensure that IEC interLATA rates cover imputed access costs. Like AT&T, BOC claims that, because an independent IEC's actual access costs are much lower than the regulated rates, an independent IEC could adopt a successful price squeeze strategy against its interexchange rivals. [FN438] BOC adds that an independent IEC may be able to increase its total profits by reducing the price of its interLATA service, thereby increasing the demand for its switched access services. [FN439]

154. The Commonwealth of the Northern Mariana Islands (CNMI) asserts that GTE owned Micronesian Telecommunications Corporation (XTC), which is the sole provider of both local exchange and exchange access services and a major provider of domestic and international off island services in the Commonwealth, currently provides domestic, interexchange services on a nondominant basis, even though it looks a separate subsidiary. CNMI asks the Commission to recognize explicitly that XTC must comply with the Fifth Report and Order separation requirements or comply with the Commission's dominant carrier requirements. [FN440] CNMI also asks the Commission to devise specific safeguards applicable to XTC's monopoly operations in the Commonwealth, such as a strengthened form of the Fifth Report and Order separation requirements. [FN441] GTE disputes CNMI's claims that XTC is providing domestic interexchange services directly as a non-dominant carrier contrary to the requirements of the Commission's Fifth Report and Order and 1996 Intercarrier Competitive Carrier Order. [FN442] GTE asserts that, although XTC provides domestic exchange, exchange access and interexchange services on an integrated basis, its domestic interexchange services are provided on a dominant basis. [FN443] GTE emphasizes that neither the Commission nor any court has found that XTC has engaged in any misconduct of the nature alleged by CNMI. [FN444] GTE also asserts that imposing additional regulatory requirements on XTC, which carries 11,000 access lines in a rural location, is clearly contrary to the deregulatory spirit and intent of the 1996 Act. [FN445].

155. CNMI also asks the Commission to clarify that XTC's service between the Commonwealth and the U.S. mainland and other U.S. points is a domestic service, and thus requires domestic facilitation and compliance with the strengthened form of the Fifth Report and Order separation requirements. [FN446] GTE responds that, because the Northern Mariana Islands have long been considered an international point for service to and from the United States, XTC currently tariffs its service to the U.S. mainland and other U.S. points in its international tariff. [FN447].

international services where an affiliated foreign carrier has the ability to discriminate against multi-linked U.S. international carriers through control of downstream services or two links in the foreign destination market. [FN532] The safeguards that we apply to carriers that we classify as dominant based on a foreign carrier affiliation are contained in Section 53.10(c) of the our rules and are designed to address the incentive and ability of the foreign carrier to discriminate in favor of its U.S. affiliate in the provision of services or facilities necessary to terminate U.S. international traffic. [FN533] This framework for discrimination issues raised by foreign carrier affiliates will apply to independent LEC's provision of U.S. international services as an additional component of our regulation of the U.S. international services market.

180. We reject NCI's suggestion that we should impose additional safeguards on the independent LEC's in-region, international services. [FN534] As we stated with regard to the FMC, all U.S. international carriers are subject to the same prohibition against exempting "special circumstances" from foreign carriers that we imposed on FCI in the O-Om approving FCI's initial 20 percent investment in NCI. [FN535]

The upcoming Subsidiary by NCI would constitute a special circumstance prohibited by the terms of Section 53.10 of the Commission's rules to the extent the U.S. carrier entered into a roaming arrangement that the foreign carrier did not offer to similarly situated U.S. carriers. [FN536] A U.S. carrier that negotiates a roaming arrangement with a foreign carrier on a point-to-point or route would be required to submit the arrangement to the Commission for public comment and review in circumstances where the arrangement deviates from existing arrangements with other U.S. carriers for the routing and/or settlement of traffic in that market. [FN537]

181. We believe our decision will benefit small incumbent LECs and small entities, for many of the same reasons enumerated in our analysis of independent LEC provision of in-region, interstate, domestic, interexchange services. For instance, by establishing a regulatory regime for provision of international services that is less burdensome for incumbent independent LECs than for RBOCs, independent LECs, many of which may be small incumbent LECs, will benefit by not being subjected to regulations that may be burdensome and may hamper competition in the international market. In addition, by limiting application of the Fifth Report and Order separation requirements to incumbent independent LECs, new entrants, some of which may be small entities, will benefit from lower market entry costs.

182. We decline to address whether NCI should be regulated as a dominant carrier for the provision of international services because of the inadequate record in this proceeding. We note that DCM or any other petitioner may petition us to initiate a proceeding regarding NCI's regulatory status. We reiterate, however, our conclusion that all independent LECs that are providing international interexchange service through an affiliate that satisfies the Fifth Report and Order separation requirements as of the date of release of this Order must continue to do so, and all other independent LECs providing international interexchange service must comply with the Fifth Report and Order separation requirements no later than one year from the date of release of this Order. [FN538]

B. Scope of Separation Requirements for Independent LECs

A. Background

183. Section 271(f)(1) of the Communications Act provides that the FCC "shall not grant an authority to any entity for three years after the date that the BOC authorizes to provide intrastate telecommunications services, unless the Commission extends such three-year period by rule or order." In the NPAK we suggested comment on whether any regulation of independent LECs should be subject to

LECs have no ability to use their bottleneck facilities to harm interexchange competition. [FN456] We believe that, absent appropriate and effective regulation, independent LECs have the ability and incentive to misallocate costs from their intraregion, interstate, interexchange services to their monopoly local exchange and exchange access services within their local service region. [FN457]

Improper allocation of costs by an independent LEC is a concern because such action may allow the independent LEC to recover costs incurred by its affiliate in providing in-region, interexchange services from subscribers to the independent LEC's local exchange and exchange access services. As we stated previously, this can deliver price signals in these markets and, under certain circumstances, may give the affiliate an unfair advantage over its competitors. [FN458]

We believe that the improper allocation of costs may cause substantial harm to consumers, competition, and production efficiency. [FN459] Such cost misallocations may be difficult to detect and are not necessarily deterred by price cap regulation.

160. Furthermore, an independent LEC, like a RBOC, potentially could use its market power in the provision of exchange access services to advantage its interexchange affiliate by discriminating against the affiliate's interexchange competitors with respect to the provision of exchange and exchange access services. [FN460] This discrimination could take the form of poorer quality interconnection or unnecessary delays in satisfying a competitor's request to connect to the independent LEC's network. [FN461]

161. We are also concerned that an independent LEC could potentially initiate a price increase to gain additional market share. [FN462] Absent appropriate regulation, an independent LEC could potentially raise the price of access to all interexchange carriers which would encourage in-region carriers to cut their retail rates, rather than maintain the same profit margins or attempt to maintain their market share by not raising their prices to reflect the increase in access charges, thereby reducing their profit margins. [FN463] If the competing in-region, interexchange providers raised their prices to recover the increased access charges, the independent LEC could seek to expand its market share by not matching the price increase. The independent LEC could also set its in-region, interexchange prices at or below its access prices. The independent LEC's in-region competitors would then be faced with the choice of lowering their retail rates, thereby reducing their profit margins, or maintaining their retail rates at the higher price and risk losing market share. [FN464]

162. As we explained earlier, the Fifth Report and Order identified three separation requirements with which an independent LEC must comply in order to qualify for regulatory treatment. These requirements are that the affiliate providing in-region, interstate, interexchange services must: (1) maintain separate books of account; (2) not jointly own transmission or switching facilities with the LEC; and (3) acquire any services from its affiliated exchange companies at fair-fair rates, terms, and conditions. [FN465]

163. We conclude today, although an independent LEC's control of exchange and interexchange services facilities may give it the incentive and ability to engage in abusive practices, unlawful discrimination, or a price squeeze, the Fifth Report and Order requirements aid in the prevention and detection of such anticompetitive conduct. We, therefore, conclude that we should retain the Fifth Report and Order separation requirements. More specifically, separate books of account are necessary to trace and document improper allocations of costs or assets between a LEC and its long distance affiliate as well as discriminatory conduct. In addition, the prohibition on jointly-owned facilities will reduce the risk of improper cost allocations of common facilities between the independent LEC and its interexchange affiliate. The prohibition on jointly owned facilities also helps to deter any discrimination in access to the LEC's transmission and switching facilities by requiring the affiliate to follow the same procedures as competing interexchange carriers to obtain access to those facilities. Finally, we conclude that requiring

(Publication page references are not available for this document.)

the local's access lines) from any separation requirements that are retained, [FM511] because the costs of imposing the separations requirements on small carriers may outweigh the likely benefits. [FM511] Several commenters argue that small, independent IECs lack the market power to engage in anticompetitive conduct that is based on their interexchange rivals. [FM513] Sprint argues that its local operations have little ability and incentive to engage in anticompetitive conduct, since its service territories are widely dispersed and largely rural. [FM514]

182. SBC and Bell Atlantic argue that there is no economic basis for exempting small or rural independent IECs from the separation requirements imposed in this Order, especially given the increasing competition in local exchange and exchange access markets throughout the country. [FM515] CIO argues that all independent IECs, small and large, generally serve areas that are less densely populated than RBOC service areas, have fewer access lines per switch on average, and provide relatively small volumes of interexchange traffic that originates and terminates in their region. [FM516]

c. Discussion

183. We conclude that we should not exempt any independent IECs from the Fifth Report and Order requirements based on the carrier's size or rural service territory because neither a carrier's size nor the geographic characteristics of the service area will affect its incentives or ability to improperly allocate costs or discriminate against rival interexchange carriers. Commenters favoring such an exemption provide no persuasive evidence that small or rural independent IECs that are not currently providing intraregion interexchange services on an integrated basis subject to dominant carrier regulation would be adversely affected by continuation of the Fifth Report and Order separation requirements or that the safeguards are unnecessary for such carriers. [FM517] Accordingly, we will continue to apply the Fifth Report and Order separation requirements to all independent IECs, regardless of size. [FM518] Furthermore, we note that, although NTCA argues that the separation requirements may cause small companies to lose market share in the form of rate recognition and good will, the Fifth Report and Order requirements do not preclude an independent IEC from taking advantage of the good will by providing interexchange services under the name of a similar name.

d. Classification of Independent IECs' Provision of In-Region, International Services

a. Background

184. In the Non Accounting Safeguards NARM we tentatively concluded that we should apply the same regulatory treatment to an independent IEC's provision of international services originating within its local service area as we adopt for independent IEC provision of interstate, domestic, interexchange services originating within its local service area. [FM519]

b. Comments

185. Most commenters support our proposal to apply the same regulatory treatment that we adopt for an independent IEC's provision of in-region interstate, domestic, interexchange services to an independent IEC's provision of in-region international services. [FM520] STF argues that the Commission should not impose

(Publication page references are not available for this document.)

The same terms and conditions as provided in an agreement approved under section 252 which the independent LEC is a party.

167. While we recognize that the Fifth Report and Order requirements impose some regulatory burdens, we find that these burdens are not unreasonable in light of the benefits these requirements yield in terms of protection against improper cost allocation, unlawful discrimination, and price squeezes. We conclude that continued imposition of the Fifth Report and Order separation requirements is necessary to prevent and combat any anticompetitive conduct that may arise as a result of an independent LEC's control of bottleneck facilities.

168. We reject GTE's contention that the 1996 Act prohibits the Commission from imposing structural safeguards on GTE or on any other independent LEC. [FN476] We find no reasonable basis for inferring from section 601, or any other provision in the 1996 Act, that Congress intended to eliminate the Fifth Report and Order requirements or to repeal by implication our authority to impose on independent LECs separation requirements that we deem necessary to protect the public interest consistent with our statutory mandate. To the contrary, section 601(c)(1) of the 1996 Act provides that we are not to presume that Congress intended to supersede our existing regulations unless expressly so provided. [FN480] Furthermore, section 501(e)(2) of the 1996 Act deals solely with a judicial decree, not the Commission's regulations; therefore, GTE's argument is frivolous.

169. We are also not persuaded by Sprint's arguments that the Fifth Report and Order requirements are no longer necessary because other Commission requirements, such as the Commission's access charge rules, regulation requirements, and cost allocation and affiliate transaction rules, prevent anticompetitive conduct by an independent LEC in providing long-distance, interstate, interexchange services. [FN481] While these other requirements have significant remedial effects, we find that these regulations alone are not an adequate substitute for the Fifth Report and Order separation requirements. As previously discussed, the prohibition against jointly owned transmission and switching facilities ensures that the affiliate may not own facilities on an equal basis. This requirement also helps to ensure that all competing long-distance providers have the same access to provisioning of transmission and switching as that provided to the independent LEC's affiliate. There is nothing in the Commission's rules that otherwise prohibit joint ownership of switching and transmission facilities. Although Sprint contends that we should impose this prohibition by modifying the cost allocation rules, [FN482] such a prohibition is possible only if a LEC provides interexchange service through a separate affiliate, as required by the Fifth Report and Order requirements. In addition, as stated previously, the Fifth Report and Order requirement that the affiliate maintain separate books of account is necessary to trace and document incorrect allocations of costs or assets between a LEC and its long distance affiliate and to detect unlawful discrimination in favor of the affiliate. [FN483] The historical purpose for the requirement that the affiliate acquire any services from its affiliated exchange companies at tariffed rates, terms, and conditions was to prevent the LEC from discriminating in favor of its long distance affiliate. [FN484]

The Commission recently reaffirmed the need for such a requirement when it applied the affiliate transaction rules to MTS transactions between dominant LECs and their affiliates. [FN485] We believe that the Commission's access charge rules, imputation requirements, and cost allocation and affiliate transaction rules continue to serve important purposes. We conclude, however, that the Fifth Report and Order requirements are also necessary under these circumstances to safeguard ratepayers against cost-shifting, discrimination, and price squeezes.

170. We reject the arguments that we should impose additional requirements on independent LECs, including section 272 requirements, certain aspects of dominant carrier regulation, or any other requirements. Independent LECs tend to be more geographically dispersed and their service territories are largely rural in nature, therefore, they generally serve areas that are less densely populated than DCC.

Order separation requirements faced by a going concern could be greater than the costs to comply with those requirements for independent LECs that are currently providing those services on a separated basis. Accordingly, Unifon, GTE Hawaiian Tel., and AT&T shall have one year from the date of release of this Order to comply with the Fifth Report and Order separation requirements. [FN501] Until that time, our Commission will continue to regulate these independent LECs as dominant carriers. The reason in this proceeding does not reflect special circumstances necessitating a waiver of one or more of these requirements. To the extent that special circumstances exist, however, independent LECs may petition us to establish the necessity of a waiver of the Fifth Report and Order requirements.

17.1. Because section 3(40) of the Communications Act defines a state to include the "Territories and possessions" of the United States, CNMI is a state for purposes of rules in telecommunications regulation. [FN502] In our Rate Integration Order, we stated that, in making the section 254(g) of the Communications Act rate integration provisions applicable to interstate interexchange services provided between the "states" as defined by section 153(10) of the Communications Act, Congress made rate integration applicable to interexchange services provided between the contiguous forty-eight states and U.S. possessions and territories, including CNMI. [FN503]

In the Rate Integration Order, we required providers of interexchange services between the Northern Mariana Islands and the contiguous forty-eight states to do so on an integrated basis with other interexchange services they provide by August 1, 1997. AT&T and all other carriers providing off-island services between CNMI and other states are required to comply with these requirements. We find no basis in the record of this proceeding to amend these requirements. We further note that, although our Rate Integration Order does not require providers of interexchange service to integrate services offered to customers in the Commonwealth until August 1, 1997, [FN504] this does not affect our finding that, if AT&T continues to provide in-region, interstate, interexchange services directly, it must continue to comply with our dominant carrier requirements prior to that date.

17.2. We find no basis on the record in this proceeding to impose additional requirements on AT&T's provision of in-region, interstate, domestic, interexchange service, beyond those applied in this Order. To the extent that CNMI or any other provider can demonstrate that AT&T has violated our rules, we encourage parties to file a petition asking the Commission to impose additional requirements through a petition for declaratory ruling or a complaint filed pursuant to section 203 of the Communications Act.

B. Application of Fifth Report and Order Separation Requirements to Non-Bell Independent LECs

i. Background

17.3. In the Net-Accounting Safeguards RRM, we tentatively concluded that, because of independent LEC's control of local exchange and exchange access facilities is our primary rationale for imposing a separate affiliate requirement on independent LECs, we should limit application of any separation requirements that we adopt in this proceeding to incumbent FCC that control local exchange and exchange access facilities. [FN505]

For purposes of determining which independent LECs are "incumbent," we proposed to use the definition of "incumbent local exchange carrier" contained in section 211(b) of the Communications Act. [FN506]

Section 251(h) provides that a LEC is an incumbent LEC, with respect to a particular area, i.e., (1) the LEC provided telephone exchange service in that area on the date of enactment of the 1996 Act (February 8, 1996), and (2) the LEC was deemed to be a member of NRCs on the date of enactment or the LEC became a successor or assign of a NRC member after the date of enactment. [FN507]

below cost without incurring a loss. According to Ameritech, any subsidies in excess are the costs that the BOC must recover in some manner in order to remain "neutral." Ameritech also claims that price squeeze arguments ignore the fact that BOC interLATA affiliates will pay access charges to unaffiliated carriers when they originate or terminate long distance calls over AT&T's and that facility-based intercarrier carriers actually have significant cost advantages. [FN256]

Fine by, however, disputes the relevance of the price squeeze arguments. According to Ameritech, a BOC interLATA affiliate's ability to gain market share by setting rates below the cost of access would not constitute a basis for classifying the BOC interLATA affiliate as dominant. [FN257]

Ameritech is aware of no legal theory under which such a practice could be considered unreasonable or otherwise unlawful, since consumers would suffer no harm unless the BOC interLATA affiliate could somehow acquire market power from the action. [FN258] Bell Atlantic and NYNEX claim that advance notice periods for tariff filings and cost support requirements are unnecessary to ensure compliance with the section 272 imputation requirement, because the 1986 Act already provides for a biennial audit, which is intended to cover specifically any slack on compliance with the section 272 requirement, including the imputation requirement. [FN259]

III. Discussion

126. In the Non-Accounting Safeguards DMR, we noted that, absent appropriate safeguards, a BOC potentially could raise its prices of access to all interexchange carriers, including its own. [FN260] This would cause competing interLATA carriers to raise their rates or incur LATA rates in order to maintain the same profit margin as the BOC. In addition, the BOC carrier would be able to raise their prices to reflect the increased access charges, thereby reducing their profits. [FN261] If the competing inter-exchange interLATA service providers raised their prices to recover the increased access charges, the BOC interLATA affiliate could seek to expand its market share by not incurring the price increases. In this event, although the BOC interLATA affiliate would achieve lower profit margins than its rivals if all other things being equal, the BOC corporate entity as a whole would enjoy an additional revenue stream from unaffiliated carriers due to the excess price increase and greater revenues from the affiliate's interLATA services caused by its increased share of interLATA traffic. If the BOC were to raise its access rates high enough, it would be impossible for interexchange competitors to compete effectively. Thus, the entry of a BOC affiliate into LATA providers of in-region, intra-state, domestic, interLATA services might give the BOC an incentive to raise the price for access services in order to disadvantage its affiliate's rivals, increase its affiliate's market share, and increase the profits of the BOC overall. [FN262]

127. We conclude, as discussed in the Notice, that price cap regulation of the BOC's access services sufficiently restricts a BOC's ability to raise access prices to a level so that the BOC affiliate would gain, upon entry or soon thereafter, the ability to raise prices of interLATA services above competitive levels by restricting the own output of those services. [FN263] Although a BOC may be able to raise its access rates to some extent if those rates are currently below the applicable price cap and could fail to pass along increases in the cost of access if the productivity factor is too low, [FN264] we conclude that such an increase would not give a BOC affiliate the ability to raise prices of interLATA services above competitive levels by restricting its own output of those services. [FN265] We will consider the impact of such a potential increase on competition in the pending access charge reform proceeding. We also note that the ability of competing carriers to acquire access through the purchase of unbundled elements enables them to avoid originating access charges and thus partially protect themselves against a price squeeze. [FN266] To the extent that access charges are reformed to more closely reflect economic cost, [FN267] as is being considered in the access charge reform proceeding, the potential for a price squeeze should be

generally eliminate the need for regulatory requirements imposed by section 214, we have granted a blanket section 214 authorization to non-dominant carriers such that they no longer must obtain price approval to provide access to long distance service or add new facilities and we impose less stringent requirements on non-dominant carriers that are discontinuing service. [FM27]

67. We recognize that certain aspects of dominant carrier regulation may constrain a BOC's ability to raise the costs of its affiliate's interLATA rivals or engage in other anticompetitive conduct. [FM28] For example, requiring a BOC telephone affiliate to file its tariffs with advance notice and cost support data might help to detect and prevent predatory pricing, particularly if coupled with a price floor on the affiliate's interLATA services. [FM29] Price cap regulation of a BOC interLATA affiliate's interLATA services may deter a BOC from raising the costs of its affiliate's rivals through discrimination or other anticompetitive conduct by limiting the profit the affiliate could earn as a result of the anticompetitive conduct. [FM30] Nevertheless, the fact that these measures might help to deter a BOC or its interLATA affiliate from engaging in certain types of anticompetitive behavior is not, by itself, a sufficient basis for increasing dominant carrier regulation on the BOC interLATA affiliates. We should also consider whether and to what extent these regulations would dampen competition and whether other statutory and regulatory provisions would accomplish the same objectives while imposing fewer burdens on the carriers and the Commission. Dominant carrier regulation should not impose on the BOC interLATA affiliates only the benefits of such regulation without the burdens that would be imposed on competition, service providers, and the Commission. [FM31]

68. The Commission has long recognized that the regulations associated with dominant carrier classification can dampen competition. [FM22] For example, advance notice procedures for tariff filing can stifle price competition and marketing innovation when applied to a competitive industry. [FM33] In the Tariff Forbearance Order, we eliminated tariff filing requirements for non-dominant carriers pursuant to our forbearance authority under the Communications Act and ordered all non-dominant interexchange carriers to cancel their tariffs for interstate, domestic, interexchange services within nine months from the effective date of the Order. [FM34]

We concluded that a regime without non-dominant interexchange carrier tariffs for interstate, domestic, interexchange services will be more market-oriented, deregulatory system. We also found that non-permitting non-dominant interexchange carriers to file tariffs with respect to interstate, domestic, interexchange services will enhance competition among providers of such services, promote competitive market conditions, and achieve other objectives that are in the public interest. [FM35]

We further concluded that continuing to require non-dominant interexchange carriers to file tariffs for interstate, domestic, interexchange services would reduce incentives for competitive price accounting, constrain carriers' ability to make rapid, efficient responses to changes in demand and cost, impose costs on carriers that attempt to make new offerings, and prevent customers from seeking out or obtaining service arrangements specifically tailored to their needs. [FM36]

69. Requiring the BOC interLATA affiliates to file tariffs on advance notice and with cost support data would impose even more significant costs and burdens on the interLATA affiliates than the one-day notice period formerly required of non-dominant carriers and would adversely affect competition. [FM37] Moreover, these requirements could undermine at least some of the benefit otherwise gained by eliminating tariff filing by non-dominant domestic interexchange carriers. In the Tariff Forbearance Order, we found that tacit coordination of prices for interstate, domestic, interexchange services, to the extent it exists, would be more difficult if we eliminate tariffs, because price and service information about such services provided by non-dominant interexchange carriers would no longer be collected and available in one central location. [FM38] After full implementation of that Order, no interexchange carrier will be obligated (or permitted) to file tariffs for interstate, domestic, interexchange services. [FM39] If we were to

price squeezing by raising prices because their access prices are regulated. [RM341] they also note that section 272(b)(2) requires BOCs to charge their affiliates the same access rates they charge unaffiliated carriers. [RM342] PacTel claims that a true price squeeze would occur only if the price charged by the BOC interLATA affiliate was less than the BOC's marginal cost of access, plus the foregone contribution from that access, plus the affiliate's cost of providing the long distance service. [RM343] PacTel contends that it would be irrational for a BOC interLATA affiliate to price below this level unless its object was predation, which is not a permissible strategy. [RM344]

On the other hand, according to PacTel, a BOC interLATA affiliate's acceptance of little or no profit in order to expand its market share, by itself, would not be a price squeeze and would not be anticompetitive. [RM345] NYNEX claims that significant changes to local exchange service and access markets initiated by the Term Competition First Report and Order make it unnecessary by law that BOC access pricing could result in local BOCs retaining long distance market power, particularly in light of the Commission's commitment to undertake and complete access reform within the next year. [RM346]

127. Non-BOC commenters generally contend that the BOCs will have the incentive and ability to engage in a price squeeze, despite price cap regulation of the BOCs' access services and other applicable safeguards. The Economic Strategy Institute asserts that antitrust and economic literature generally supports the need for regulatory intervention in cases of price squeezes. [FN347] MCI contends that the BOCs are most likely to exercise market power by assessing excessive prices for exchange access services for all carriers (including the BOCs' interLATA affiliates), [RM348] and price cap regulation will not prevent this tactic because access rates are already excessive. [RM349] MCI argues that, as long as a BOC is allowed to provide both essential services and competitive services, and as long as those essential services are priced above cost, a vertically integrated BOC can drive even more efficient rivals out of the market. [RM350] MFS and MCI further assert that a price squeeze would not be limited to price increases in access services, but could also arise from the contribution BOCs earn on stimulated demand for access services created by competing local telephone price reductions to match a BOC interLATA affiliate price reduction. [RM351] MCI claims that such a strategy could seriously harm competition. According to MCI, even if rivals remain in the market, they will be weakened by the cost increases they are forced to absorb, thereby reducing their output and the "vigor of competition." [RM352]

128. BOCs assert that the structural separation, accounting, and fugitation requirements in the Communications Act do not adequately address the BOCs' access cost advantage because: (1) there is no way to ensure that a BOC interLATA affiliate's costs, other than for access, are reflected in its prices; (2) to the extent customers buy bundled local exchange, long distance, and other services from a BOC interLATA affiliate, the BOC interLATA affiliate could effectively evade fugitation requirements by passing on the access cost advantage in reduced prices for services not subject to the Commission's direct jurisdiction, such as local exchange and interconnection services; (3) a BOC will have the incentive and ability to favor its interLATA affiliate over its competitors in the provision of bundled local exchange and interLATA services; and (4) a BOC has the ability to discriminate against its affiliate's interLATA competitors on terms other than price. [RM353]

129. MCI and RSWT argue that requiring cost support data and advance notice periods for tariff filings is important to ensure that the BOC interLATA affiliates are pricing their services above their costs. [FN354] MFS, however, questions whether tying BOC interLATA affiliates as dominant firms would be effective in preventing price squeezes. It contends that the only effective mechanisms for preventing this behavior are pricing BOC essential services at economic cost and developing competitve alternatives to the BOCs' essential services. [RM355]

130. Ameritech disputes arguments that access charges are priced above economic cost and therefore will cause BOC interLATA affiliates to set interLATA rates

bottleneck facilities. [FN246] We sought comment on the application of these factors in determining whether the BOC interLATA affiliates should be classified as dominant or non-dominant.

vi. Comments

94. Most commenters that address the issue agree that each of the traditional market factors weighs in favor of classifying the BOC interLATA affiliates as non-dominant. [FN247] According to Ameritech, it is inconceivable that a BOC interLATA affiliate "could bring AT&T to its knees quickly" because the affiliates will enter the long distance market with no customers, no traffic, no revenues, and no cross-subsidized lines and will be competing against more than 500 telephone carriers, including AT&T, SBC and Sprint, all of which are well-established in the market. [FN248] Ameritech and S&S West also claim that, in considering whether to classify the BOC interLATA affiliates as dominant, the Commission should consider only whether the BOC interLATA affiliates will have market power upon entry, not whether they will quickly gain such market power. [FN249]

95. The California Bell Telephone Association (CTA) contends, however, that a BOC interLATA affiliate's initial zero market share should not dissuade the Commission from requiring dominant carrier regulation because, as an entity affiliated with the dominant provider in the state, it will have enormous advantages particularly in terms of brand identification. CTA further argues that it is likely that these affiliates will seek to capitalize on their parental lineage by using some or all of the BOC's logos or other branding mechanisms. [FN250] EDG asserts that market share is and at times is not a measure of market power, but rather is one of many possible indications that market power may exist in a certain market. [FN251]

vii. Discussion

96. We find that each of the traditional market factors (excluding bottleneck facilities) supports a conclusion that the BOC interLATA affiliates will not have the ability to raise price by restricting their output upon entry or soon thereafter. As stated in the Notice, the fact that each BOC interLATA affiliate initially will have zero market share in the provision of intra-region, interstate, domestic interLATA services suggests that the affiliate will not initially be able to raise price by restricting its output. [FN252] As discussed in the Notice, however, we find that this factor is not conclusive in determining whether a BOC interLATA affiliate should be classified as dominant, because the affiliate's zero market share results from its exclusion from the market until now, and, the affiliate potentially could gain significant market share upon entry or shortly thereafter, because of its brand identification with intra-region customers, possible efficiencies of integration, and the FCC's ability potentially to raise the costs of its BOC interLATA rivals.

97. As to supply substitutability, we note that the Commission has previously found that the excess capacity of AT&T's competitors is sufficient to constrain AT&T's exercise of market power. [FN253] In light of that finding, we conclude that AT&T and its competitors, which currently serve all interLATA customers, should be able to expand their capacity sufficiently to attract a BOC interLATA affiliate's customers if the affiliate attempts to raise its interLATA prices. [FN254] As we discussed in the Notice, the Commission has also found that the purchasing decisions of most customers of domestic interexchange services are sensitive to changes in price, and customers would be willing to shift their traffic to an interexchange carrier's rival if the carrier raises its prices. [FN255] The existence of such demand substitutability supports

to such an extent that the affiliate would gain the ability to raise prices by restricting its own output upon entry or shortly thereafter.

117. The 1996 Act contains a number of nondiscrimination safeguards, which we have implemented in the Non Accounting Safeguards Order and Accounting Safeguards Order. For example, section 272(c)(1) prohibits a BOC, in its dealings with its another 272 affiliate, from "discriminating between that company or affiliate and any other entity in the provision or procurement of goods, services, facilities, and information, or in the establishment of standards." [FN315] To the Non-Accounting Safeguards Order, we concluded that section 272(c)(1) requires a BOC to provide unaffiliated entities the same goods, services, facilities, and information that it provides to its section 272 affiliate at the same rates, terms, and conditions. [FN316] We also concluded that a prima facie case of discrimination would exist under section 272(c)(1) if a BOC does not provide unaffiliated entities the same goods, services, facilities, and information that it provides to its section 272 affiliate at the same rates, terms, and conditions. [FN317] In addition, we would expect that to the extent a BOC develops new services for or with a non-section 272 affiliate, it must develop new services for or with unaffiliated entities in the same manner. [FN318]

118. Section 272(e) also imposes a number of specific nondiscrimination requirements. For example, section 272(e)(1) requires a BOC to "fulfill any requests from an entity's interexchange for telephone exchange service and exchange access within a period no longer than the period in which it provides such telephone exchange service and exchange access to itself or its affiliates." [FN319] In the Non-Accounting Safeguards Order, we concluded that the term "requests" includes, but is not limited to, initial installation requests, subsequent requests for improvements, upgrades or modifications of service, or repair and maintenance of those services. [FN320] We also concluded that BOCs must disclose to unaffiliated entities information regarding service intervals in which BOCs provide service to interexchange or their affiliates. [FN321] This disclosure requirement should promote compliance with section 272(e)(1) and allow competitors to resolve disputes informally rather than using the Commission's formal complaint process. [FN322]

119. Section 272(e)(3) restricts the ability of a BOC to provide "facilities, services, or information concerning its provision of exchange access to [its affiliate], unless [it makes] such facilities, services, or information ... available to other providers of interLATA services in that market on the same terms and conditions." [FN323] Coupled with existing equal access and network disclosure requirements, this provision will limit the BOCs' ability to discriminate in the provision of such facilities, services, and information.

120. Section 272(e)(2) requires that a BOC charge its affiliate "an amount for access to its telephone exchange service and exchange access that is no less than the amount [that the BOC charges] any unaffiliated interexchange carrier for such service." [FN324] In the Non-Accounting Safeguards Order, we recognized that this provision serves to constrain a BOC's ability to engage in discriminatory pricing of its exchange and exchange access service. [FN325]

121. We also find that the structural separation requirements of section 272(e) will constrain a BOC's ability to discriminate against its affiliate's interLATA competitors. As previously noted, we have interpreted the section 272(e)(1) requirement that a section 272 entity "operate independently" from the BOC to prohibit the joint ownership of transmission and switching facilities by the BOC and its affiliate. [FN326] This requirement ensures that an affiliate must obtain any such facilities on an arm's length basis pursuant to section 272(e)(2), thereby increasing the transparency of transactions between a BOC and its affiliate. [FN327] As we observed in the Non-Accounting Safeguards Order, "[t]ogether, the prohibition on joint ownership of facilities and the nondiscriminatory requirements should ensure that competitors can obtain access to transmission and switching facilities equivalent to that which section 272

to date indicates that such competition is still in its infancy. As a result, we conclude, solely for purposes of this proceeding, that the BOCs currently possess market power in the provision of local exchange and exchange access services in their respective regions, and we therefore must consider whether they can use that market power to give their interLATA affiliates the ability to raise the prices of inter-region, interstate, domestic, interLATA services by restricting their own output of those services.

ii. Improper Allocation of Costs

i. Commerce

(C). The BOCs and USIA assert that statutory and regulatory safeguards should prevent any improper cost allocations from occurring, particularly because all BOCs are subject to price cap regulation, and a majority have adopted the no sharing option. [FN263] AT&T asserts that the concern over improper cost allocation ignores current regulation of the BOCs and presumes the incompetence of both state and federal regulators. [FN264] AT&T counters that price cap regulation cannot eliminate the incentive to allocate costs improperly because both the initial caps and subsequent adjustments are generally set at least in part on the basis of the BOC's profits during the preceding years. [FN265] The Economic Strategy Institute asserts that cost accounting methodologies and models leave room for manipulation and infringement. [FN266] It also claims that improper cost allocation can lead to substantial cost advantages and facilitate a price squeeze. [FN267]

(C). The BOCs and USIA contend that it defies economic sense to expect any of the BOC interLATA affiliates to drive AT&T, SBC, or Sprint from the long distance markets. Even if they could, these commenters assert, the fact is that neither BOC remains intact, ready for another firm to buy at distress sale prices. [FN270] AT&T, CCA, and BOC argue, however, that the concerns expressed in the NPMC regarding improper cost allocation are unfounded. In addition to raising the possibility of predatory pricing, improper cost allocation may cause substantial harm to consumers, competition, and production efficiency. [FN271] For example, improper cost allocation could force higher prices for local exchange and exchange access services and could shift market share and profits to a BOC interLATA affiliate, even if the affiliate is less efficient than its competitors, thereby resulting in a loss of production efficiency. [FN272] AT&T asserts that such a strategy would be costless to the BOC, for it would recover its losses in the competitive market through contemporaneous higher rates in the non-competitive market. As a result, no subsequent recompence would be necessary. [FN273] According to BOC, the Commission must consider whether applicable regulation would prevent improper cost allocation that would result in sheer adverse effects on consumers, competition, and production efficiency. BOC argues that regulation alone will not prevent competitively significant improper cost allocations. The incentives to engage in such practices, according to BOC, will be minimized only when the local exchange market is subject to robust competition. [FN274].

ii. Deregulation

(C). As noted in the Non-Accounting Safeguards XPRM, improper allocation of costs by a BOC is of concern because such action may allow a BOC to recover costs from subscribers to its regulated services that were incurred by its interLATA affiliate in providing competitive interLATA services. In addition to the direct harm to regulation payers, this practice can distort price signals in those markets and

basic service rates, thus reducing the incentive for the BOCs to shift nonregulated costs to regulated services." [PN287] We recognize that under our current interim rate price cap rules, a BOC can select an X-factor option that requires it to share interstate earnings with its customers that exceed specified benchmarks and permit the BOC to make a low-end adjustment if interstate earnings fall below a specified threshold. [PN288]

Consequently, in certain circumstances, a BOC may have an incentive to allocate costs from interLATA services to access services in order to reduce the amount of profits the BOC is required to share with its interstate access service customers or become eligible for a low-end adjustment. [PN289]

We note, however, that only one of the BOCs currently has adopted a sharing option. [PN290] Our affiliate transaction rules, which apply to transactions between the BOCs and their interLATA affiliates, [PN291] should make it more difficult for a BOC to allocate improperly the costs of its affiliates' interLATA services. We also recognize that, if a state does not impose price cap regulation on a BOC's local exchange services, the BOC may have an incentive to allocate costs from interLATA services to its local exchange services. It appears, however, that many states have adopted price cap regulation or some other alternative form of regulation for the BOC's local exchange services. [PN292] Moreover, we are not persuaded that dominant carrier regulation of the BOC interLATA affiliates' interLATA services will prevent such improper cost allocation.

107. Furthermore, even if a BOC were able to allocate improperly the costs of its affiliate's interLATA services, we conclude that it is unlikely that a BOC interLATA affiliate could engage successfully in predation. [PN293] AT&T, SPRINT, and MCI WorldCom -- have nationwide, or near-nationwide, network facilities that cover every BOC region. [PN294] These are large well-established companies with millions of consumers throughout the nation. It is unlikely, therefore, that a BOC interLATA affiliate, whose customers are likely to be concentrated in the BOC's local service region, [PN295] could drive the majority of those national companies from the market. Even if it could do so, it is doubtful that the BOC interLATA affiliate would later be able to raise prices in order to recoup lost revenues. [PN296] As Professor Spulber has observed, "[i]n even in the unlikely event that [a BOC interLATA affiliate] could drive one of the major long distance carriers into bankruptcy, the fiber-optic transmission capacity of that carrier would remain intact, ready for another firm to buy the capacity at distress sale and immediately undercut the affiliate's downstream service prices." [PN297]

108. We acknowledge that improper cost allocation may raise concerns beyond the risk of predatory pricing. As AT&T and BOC assert, exploiting improper cost allocation to divert business to BOC interLATA affiliates from other, more efficient suppliers would be anticompetitive even if the latter supplier were free in the market. [PN298]

DOJ contends that this strategy would produce inefficiencies and wasted resources and reduce future investment by competitors to improve or expand their networks and to develop innovative technologies and services. [PN299] AT&T claims that such a strategy would be costless to the BOC.

109. It would recover its losses in the competitive market through contemporaneous higher rates in the non-competitive market, and, consequently, subsequent recuperation would be unnecessary. [PN300] As previously stated, although we agree that these are serious concerns, we find that they do not establish a persuasive basis for classifying the BOC interLATA affiliates as dominant in the provision of intra-region, interstate, domestic, interLATA services. Rather, such concerns are best addressed through enforcement of the section 270 requirements. We also note that DOJ contends that dominant carrier regulation will not prevent the BOCs from improperly allocating their affiliates' interLATA costs. In fact, DOJ asserts that the incentives to engage in such practices will be eliminated only when the local exchange market is subject to robust competition. [PN301] As previously discussed, we conclude that dominant carrier regulation generally would not help prevent a BOC from improperly allocating costs. [PN302]